

Act of 1974 (the Act) provides that a plan may not acquire any qualifying employer security or qualifying employer real property, if immediately after such acquisition the aggregate fair market value of qualifying employer securities and qualifying employer real property held by the plan exceeds 10 percent of the fair market value of the assets of the plan.

(b) *Acquisition.* For purposes of section 407(a) of the Act, an acquisition by a plan of qualifying employer securities or qualifying employer real property shall include, but not be limited to, an acquisition by purchase, by the exchange of plan assets, by the exercise of warrants or rights, by the conversion of a security (except any acquisition pursuant to a conversion exempt under section 408(b)(7) of the Act), by default of a loan where the qualifying employer security or qualifying employer real property was security for the loan, or by the contribution of such securities or real property to the plan. However, an acquisition of a security shall not be deemed to have occurred if a plan acquires the security as a result of a stock dividend or stock split.

(c) *Fair market value—Indebtedness incurred in connection with the acquisition of a plan asset.* In determining whether a plan is in compliance with the limitation on the acquisition of qualifying employer securities and qualifying employer real property in section 407(a)(2), the limitation on the holding of qualifying employer securities and qualifying employer real property in section 407(a)(3) and § 2550.407a-3 thereunder, and the requirement regarding the disposition of employer securities and employer real property in section 407(a)(4) and § 2550.407a-4 thereunder, the fair market value of total plan assets shall be the fair market value of such assets less the unpaid amount of:

(1) Any indebtedness incurred by the plan in acquiring such assets;

(2) Any indebtedness incurred before the acquisition of such assets if such indebtedness would not have been incurred but for such acquisition; and

(3) Any indebtedness incurred after the acquisition of such assets if such indebtedness would not have been incurred but for such acquisition and the incurrence of such indebtedness was

reasonably foreseeable at the time of such acquisition. However, the fair market value of qualifying employer securities and qualifying employer real property shall be the fair market value of such assets without any reduction for the unpaid amount of any indebtedness incurred by the plan in connection with the acquisition of such employer securities and employer real property.

(d) *Examples.* (1) Plan assets have a fair market value of \$100,000. The plan has no liabilities other than liabilities for vested benefits of participants and does not own any employer securities or employer real property. The plan proposes to acquire qualifying employer securities with a fair market value of \$10,000 by paying \$1,000 in cash and borrowing \$9,000. The fair market value of plan assets would be \$100,000 (\$100,000 of plan assets less \$1,000 cash payment plus \$10,000 of employer securities less \$9,000 indebtedness), the fair market value of the qualifying employer securities would be \$10,000, which is 10 percent of the fair market value of plan assets. Accordingly, the acquisition would not contravene section 407(a).

(2) Plan assets have a fair market value of \$100,000. The plan has liabilities of \$20,000 which were incurred in connection with the acquisition of those assets, and does not own any employer securities or employer real property. The plan proposes to pay cash for qualifying employer securities with a fair market value of \$10,000. The fair market value of plan assets would be \$80,000 (\$100,000 of plan assets less \$10,000 cash payment plus \$10,000 of employer securities less \$20,000 indebtedness), the fair market value of the qualifying employer securities would be \$10,000, which is 12.5 percent of the fair market value of plan assets. Accordingly, the acquisition would contravene section 407(a).

[42 FR 47201, Sept. 20, 1977]

§ 2550.407d-5 Definition of the term “qualifying employer security”.

(a) *In general.* For purposes of this section and section 407(d)(5) of the Employee Retirement Income Security Act of 1974 (the Act), the term “qualifying employer security” means an employer security which is:

(1) Stock; or

(2) A marketable obligation, as defined in paragraph (b) of this section and section 407(e) of the Act.

(b) For purposes of paragraph (a)(2) of this section and section 407(d)(5) of the Act, the term “marketable obligation” means a bond, debenture, note, or certificate, or other evidence of indebtedness (hereinafter in this paragraph referred to as “obligation”) if:

(1) Such obligation is acquired—

(i) On the market, either—

(A) At the price of the obligation prevailing on a national securities exchange which is registered with the Securities and Exchange Commission, or

(B) If the obligation is not traded on such a national securities exchange, at a price not less favorable to the plan than the offering price for the obligation as established by current bid and asked prices quoted by persons independent of the issuer;

(ii) From an underwriter, at a price—

(A) Not in excess of the public offering price for the obligation as set forth in a prospectus or offering circular filed with the Securities and Exchange Commission, and

(B) At which a substantial portion of the same issue is acquired by persons independent of the issuer; or

(iii) Directly from the issuer at a price not less favorable to the plan than the price paid currently for a substantial portion of the same issue by persons independent of the issuer;

(2) Immediately following acquisition of such obligation,

(i) Not more than 25 percent of the aggregate amount of obligations issued in such issue and outstanding at the time of acquisition is held by the plan, and

(ii) At least 50 percent of the aggregate amount referred to in paragraph (A) is held by persons independent of the issuer; and

(3) Immediately following acquisition of the obligation, not more than 25 percent of the assets of the plan is invested in obligations of the employer or an affiliate of the employer.

[42 FR 44388, Sept. 2, 1977]

§ 2550.407d-6 Definition of the term “employee stock ownership plan”.

(a) *In general*—(1) *Type of plan*. To be an “ESOP” (employee stock ownership plan), a plan described in section 407(d)(6)(A) of the Employee Retirement Income Security Act of 1974 (the Act) must meet the requirements of this section. See section 407(d)(6)(B).

(2) *Designation as ESOP*. To be an ESOP, a plan must be formally designated as such in the plan document.

(3) *Retroactive amendment*. A plan meets the requirements of this section as of the date that it is designated as an ESOP if it is amended retroactively to meet, and in fact does meet, such requirements at any of the following times:

(i) 12 months after the date on which the plan is designated as an ESOP;

(ii) 90 days after a determination letter is issued with respect to the qualification of the plan as an ESOP under this section, but only if the determination is requested by the date in paragraph (a)(3)(i) of this section; or

(iii) A later date approved by the Internal Revenue Service district director.

(4) *Addition to other plan*. An ESOP may form a portion of a plan the balance of which includes a qualified pension, profit-sharing, or stock bonus plan which is not an ESOP. A reference to an ESOP includes an ESOP that forms a portion of another plan.

(5) *Conversion of existing plan to an ESOP*. If an existing pension, profit-sharing, or stock bonus plan is converted into an ESOP, the requirements of section 404 of the Act, relating to fiduciary duties, and section 401(a) of the Internal Revenue Code (the Code), relating to requirements for plans established for the exclusive benefit of employees, apply to such conversion. A conversion may constitute a termination of an existing plan. For definition of a termination, see the regulations under section 411(d)(3) of the Code and section 4041(f) of the Act.

(6) *Certain arrangements barred*—(i) *Buy-sell agreements*. An arrangement involving an ESOP that creates a put option must not provide for the issuance of put options other than as provided under § 2550.408b-3 (j), (k) and (l). Also, an ESOP must not otherwise obligate